1996 U.S. REGION PRICING STRUCTURE
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PROPOSAL

To adopt the 1996 U.S. Region Pricing Structure described below to be effective January 1996.
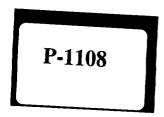
BACKGROUND

Recognizing the accelerating pace of the consolidation of the credit and debit card processing businesses, MasterCard is proposing to alter its transaction processing pricing methodology in order to compensate MasterCard for the value it brings to the membership for all transactions, whether it processes them or not, and to competitively price transaction processing fees. MasterCard is also proposing to significantly modify its assessment tiers to reward member growth. The result of these changes in transaction pricing and assessments continues MasterCard's movement toward collecting a higher percentage of its fees from transaction pricing.

MasterCard currently processes 92% of its transaction volume. It is paid an average of 4.8¢ for each one of the transactions it processes. MasterCard currently does not process 8% of its transactions - 3% are on-us transactions and 5% are bilateral and intraprocessor transactions. MasterCard receives no revenue from bilateral and intraprocessor transactions.

Whether a transaction is processed by MasterCard or not, the transaction utilizes the MasterCard brand and thereby is afforded an array of MasterCard operational services, including:

- MasterCard liability coverage in the event of member failure
- 24 hour global access for every issuer
- Stand-in for every issuer
- Unlimited capacity and the ability to handle all volume.

Increasing consolidation of credit and debit card processors heightens the possibility of a significant increase in MasterCard volume being processed outside the MasterCard processing system at some point in time.

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ANALYSIS

I. Assessments

MasterCard is proposing to modify its issuer assessment tiers in 1996 to reward member growth and support of the MasterCard brand.

MasterCard is proposing keeping its assessment tier rates constant. With respect to tier volume levels, aggregate volume levels in the first three tiers would be raised below the anticipated growth in MasterCard volume. Tier 4, 5 and 6 volume levels will not be raised at all. The result of this pricing will be to allow members to significantly grow their MasterCard sales volumes with a nominal increase in overall assessment fees paid to MasterCard. To illustrate, an average top 50 MasterCard member growing its volume 18% would pay MasterCard only 2% more in issuer assessment fees.

The attached Addendum A details the proposed assessment tiers for 1996.

II. Transaction Processing

The membership has invested a great deal of money building the MasterCard Banknet system and the architecture it requires to support peak member volume. MasterCard must maintain the size and efficiency of Banknet, and grow it at a pace that keeps up with industry volume growth, because of MasterCard's role as the stand-in processor for issuers. As a result of MasterCard's obligation to its membership to provide the aforementioned level of support, Banknet costs are more than 80% fixed. However, MasterCard's current transaction pricing is over 96% variable. Therefore, selective, reduced use of the network impacts transaction processing revenue and expense distribution across the remaining transactions.

MasterCard is proposing to address these issues by altering its pricing structure. Under the proposed structure, MasterCard will charge a "Network Access and Brand Usage" fee on all transactions processed under the MasterCard brand, whether processed by MasterCard or not. This fee will be reduced on incremental volume for MasterCard's largest volume producers as they cross the threshold for covering MasterCard's fixed expenses. In addition, MasterCard will move from its historical pricing philosophy of charging every member, regardless of size, the same price for authorization and settlement, to a tiered pricing schedule that incents member volume. The larger a member is, in terms of processing volume, the lower the member's unit price will be.

MasterCard is also proposing to substantially increase the connectivity fee paid by processors to MasterCard. Rather than charging to recover only MIP expenses, MasterCard will charge to cover MIP expenses and a portion of the capacity and stand-in expenses it incurs to support the processors' volumes. MasterCard will also implement a minimum connectivity fee for principal members who are not processors to partially cover the cost of maintaining their files and data at MasterCard.

The following chart showing MasterCard's revenue per item in 1995 vs. 1996 demonstrates the results of the proposed structural change.

MasterCard Revenue Per Transaction

	1995			1996	
	Trans. Proc. By MC	Trans. Not Proc. By MC		Trans. Proc. By MC	Trans. Not Proc. By MC
Issuer	4.2¢	0	Issuer		
Acquirer	0.5¢	0	"Brand Usage" (1)	1.67¢	1.67¢
Processor	0.1¢	0.1¢	Processing (1)	1.93¢	0
MasterCard	4.8¢	0.1¢	New Fees (2)	0.30¢	0.30¢
Revenue			Subtotal Issuers	3.90¢	1.97¢
			Acquirer (3)	0.5¢	0.5¢
			Processor	0.4¢	0.4¢
			MasterCard Revenue	4.8¢	2.9¢

(1) Average Pricing differences by member exist due to financial detail record ratios, processing size and member size.
(2) New fees from on-us and intraprocessor/bilateral Network Access and Brand Usage fees on transactions not previously processed by MasterCard, e.g., intraprocessor, bilateral or on-us transactions.
(3) Acquirer access fees remain unchanged, except they will be charged on all MasterCard transactions whether processed by MasterCard or not.

Overall, MasterCard revenue per transaction remains approximately the same. Issuer costs per transaction fall from 4.2¢ to 3.9¢ on all transactions, but due to volume tiering, issuing members would pay from 2.8¢ to 4.3¢ on their last incremental transaction.

III. Processing Record Charges

In addition to restructuring its transaction processing pricing structure, MasterCard is proposing to begin charging for all its processing records. MasterCard historically charged for all its records, but a few recent additional records (in years 1993 and 1994) have not been priced. The only record for which there would be a new charge having any consequential volume is the 635 record. The 635 record is used to collect enhanced data on financial transactions. Currently, virtually all the 635 volume is generated by Interchange Compliance. MasterCard currently uses the 635 record to match millions of transactions a day to ensure they are being processed at the appropriate interchange rate. As a result of instituting this program in October 1994, issuers are being paid an additional $75 million per year by acquirers and merchants. The cost to the issuing members of processing the more than 2 billion 635 records required yearly for Interchange Compliance will be $15 million in 1996. This equates to approximately 0.67¢ additional per transaction, but the impact will vary by member depending on its size.

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The following chart illustrates what the change would be from 1995 to 1996 in the cost of an incremental transaction for members representing a range of issuing volumes. The 1996 costs reflect the structural change described above as well as the charge for the 635 record.

Issuing Member Cost Per Incremental Transaction
Including 635 Record in 1996

	1995	1996
Member With Very Large MasterCard Volume	4.2¢	3.3¢
Member With Large MasterCard Volume	4.2¢	4.2¢
Member With Small MasterCard Volume	4.2¢	5.1¢

The variance ranges to ±20% on these incremental transactions. When weighted across total fees and assessments the median increase is 4%.

The attached Addendum B details the new transaction processing pricing structure for 1996.

IV. Supermarket and Warehouse Club Pricing

MasterCard has special interchange rates and marketing support fees for large new acceptance categories that historically did not accept credit cards. The two categories at present are supermarkets and warehouse clubs.

The current supermarket marketing support fee is 0.0015% per dollar spent (down from the original 0.002%). This fee was adopted to support marketing and promotion expense for this new acceptance category. MasterCard is proposing a fee of 0.002% for all warehouse club transactions to support the marketing and promotion expense of this new acceptance category.

MasterCard is also proposing to modify the way it collects these fees. Under this proposal, fees would be collected on all supermarket and warehouse transactions, according to merchant category (i.e., MCC 5411 for supermarkets and MCC 5300 for warehouse clubs), without regard to whether the transactions qualify for the supermarket or warehouse interchange rate. This change will provide MasterCard with funding to support marketing and promotional activity for the new categories appropriately based upon whether the transaction originated in the category.

V. Summary

In total, this new fee structure rewards those who significantly contribute to MasterCard's volume and support the brand. For the first time, MasterCard will reward not only assessment, but processing volume as well, with incrementally lower rates.

MasterCard also continues the trend towards collecting a greater percentage of its fees from processing activity and less from assessments. Finally, under the new structure, MasterCard will now be compensated with a Network Availability and Brand Usage Fee for all transactions that utilize the MasterCard brand.

The proposed pricing changes raise MasterCard's fees approximately $21MM in 1996 over 1995. Assuming anticipated growth, MasterCard will earn $1.8MM more in assessment fees, $19MM more in transaction fees for pricing and $0.5MM more in supermarket fees.

In consideration of the foregoing, the Board is asked to adopt the following resolution.

RESOLVED, that the U.S. pricing structure and fee recommendations be and hereby are, approved for implementation in 1996, as presented to the U.S. Region Board of Directors.

1996 U.S. Region Issuer Assessment Tiers

Tier	Increment	Proposed 1996 Volume (000)	Tier Volume Growth Over 1995	Proposed 1996 Rate	Tier Rate Growth Over 1995
1	first	132,000	22%	$0.79	0%
2	next	385,000	14%	$0.69	0%
3	next	440,000	5%	$0.59	0%
4	next	419,000	0%	$0.49	0%
5	next	2,324,000	(4)%	$0.39	0%
6	over	3,700,000	0%	$0.29	0%

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1996 U.S. Region Transaction Processing Fees
Affected by the New Pricing Structure

Network Access and Brand Usage Fee - progressive tiers by month, by member, paid by the issuer

Rate	Financial Detail Record Volume (000)
$0.018	0-10,000
$0.013	10,001 and up

Settlement - progressive tiers by month, by member, paid by the issuer

Rate	Settlement Record Volume (000)
$0.0084	0 - 3,000
$0.0067	3,001 - 9,000
$0.0060	9,001 - 18,000
$0.0055	18,001 - 36,000
$0.0050	36,001 and up

Authorization - progressive tiers by month, by member, paid by the issuer

Rate	Issuer Authorization Volume (000)
$0.0110	0 - 1,000
$0.0080	1,001 - 3,000
$0.0075	3,001 - 6,000
$0.0070	6,001 - 12,000
$0.0065	12,001 - and up

Processor Connectivity - paid by the processor

Rate
$5,000 per month, per MIP

Member Connectivity - paid by members who are not processors (members who do not have MIPS)

Rate
$500 per month, per member

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